United States - Transitional Safeguard Action on Combed Cotton Yarn from Pakistan

Answers to Written Questions from the Panel

1. The United States is pleased to respond to the written questions posed by the Panel. The United States notes that several of these questions involve interpretations of WTO agreements other than the WTO *Agreement on Textiles and Clothing* ("ATC"). Although the United States provides below full responses to all the questions presented by the Panel relating to non-transitional WTO agreements, the United States notes its strongly held view that it is not appropriate to attribute to the text of the ATC language or interpretations from other agreements.

2. As the United States discussed in its first written submission, the text, object and purpose of the ATC differ significantly from those of the non-transitional WTO agreements.[1] The ATC is a special transitional agreement designed to integrate the textiles and clothing sector into the disciplines of the *General Agreement on Tariffs and Trade 1994* ("GATT") over a ten-year period. The ATC derives from neither the GATT nor any other WTO agreement; rather, the ATC is the carefully negotiated successor to the Multifiber Arrangement ("MFA"), which served as the model for and informs the context of the ATC.[2] It is therefore not surprising that the text of the Article 6 transitional safeguard – particularly with respect to the "domestic industry producing like and/or directly competitive products" – reflects the unique purpose of the ATC and, in turn, is different from other WTO agreements.

3. Most importantly, as the Appellate Body recognized, the ATC – particularly Article 6 – sets forth a carefully negotiated balance of rights and obligations between exporting and importing Members.[3] It would be inappropriate to impute words, concepts, and interpretations of non-transitional agreements into the carefully negotiated balance of the ATC. Instead, the United States would urge the Panel to remain, as the Appellate Body has discussed, within the "four corners"of the ATC[4] and interpret Article 6 as it applies to the facts of this case based on the unique text of Article 6 considered in light of the object and purpose of the ATC.[5]

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[1] First written submission of the United States, ¶¶ 37-43, 57-63.

[2] The Appellate Body clearly recognized that the prior existence and demise of the MFA informs the context of the ATC. *United States - Restrictions on Imports of Cotton and Man-Made Fibre Underwear*, WT/DS24/AB/R, Report of the Appellate Body, 25 February 1997, at p. 16 ("Report of the Appellate Body, *United States - Underwear*").

[3] *United States – Measures Affecting Imports of Woven Wool Shirts and Blouses from India*, WT/DS33/AB/R, Report of the Appellate Body, 25 April 1997, at p. 19 ("Report of the Appellate Body, *United States – Wool Shirts*"). See also Report of the Appellate Body, *United States - Underwear*, at 15.

[4] The Appellate Body has stressed the importance of interpreting the ATC within its four corners and not based on other agreements. *See* Report of the Appellate Body, *United States – Underwear*, at 12, 13 (criticizing the Panel for going "outside the four corners of the *ATC*" to address a question answerable within Article 6) *and* Report of the Appellate Body, *United States – Wool Shirts*, at 19 (rejecting the relevance of certain GATT 1947 panel reports and stressing that Article 6 should be interpreted as an integral part of the ATC's transitional mechanism).

[5] Report of the Appellate Body, *United States - Underwear*, at p. 14.

Question 1: *With respect to the scope of the subject domestic industry, please discuss the ... findings of the Appellate Body in Korea - Taxes on Alcoholic Beverages (DS 75 and 84) [contained in paragraphs 114, 115, 120].*

4. In *Korea - Taxes on Alcoholic Beverages*, the Appellate Body was called upon to interpret the phrase "directly competitive or substitutable product" for purposes of *Ad* Article III:2 of the GATT 1994. Based on these findings, the Panel has asked that Parties to conduct a "comparative analysis" of the term "directly competitive products" under the ATC and elsewhere for purposes of the determining the scope of the subject domestic industry.

5. The United States believes that, as applied to the facts of this case,[6] the interpretive framework set out by the Appellate Body in *Korea - Taxes on Alcoholic Beverages* is of some, but limited use, in considering the U.S. identification of the combed cotton yarn for sale industry as the relevant domestic industry for purposes of Article 6 of the ATC. Combed cotton yarn establishments produce combed cotton yarn for sale on the marketplace. This combed cotton yarn is a "directly competitive product" with imports of combed cotton yarn. By contrast, vertically integrated producers of fabric do not produce a "directly competitive product." Combed cotton yarn manufactured by vertically integrated establishments is consumed internally, is not intended for release onto the market, and does not compete with imports of combed cotton yarn on the marketplace.

6. The Appellate Body's findings in *Korea - Taxes on Alcoholic Beverages* confirm that the ordinary meaning of "directly competitive" turns largely on whether the imported and domestic products compete with each other in the *marketplace*: "[t]he term 'directly competitive or substitutable' describes a particular type of relationship between two products...[t]he context of the competitive relationship is necessarily the *marketplace* since this is the forum where consumers choose between different products."[7] (emphasis supplied) The Appellate Body went on to find, based largely on the word "substitutable," that "directly competitive or substitutable" also involves an analysis beyond current consumer preferences, such as alternative ways of

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[6] The Appellate Body recognized that an assessment of "directly competitive" must account for the relevant facts in each case. *Japan - Taxes on Alcoholic Beverages*, WT/DS8/R/AB, Report of the Appellate Body, 4 October 1996, at p. 25 ("Report of the Appellate Body, *Japan - Alcohol*"). Therefore, the Panel must pay close attention to the facts and circumstances of this case and should avoid any invitation to engage in speculation concerning hypothetical facts or scenarios, particularly those outside the scope Market Statement.

[7] *Korea - Taxes on Alcoholic Beverages*, WT/DS75/AB/R, Report of the Appellate Body, 18 January 1999, at ¶ 114 ("Report of the Appellate Body, *Korea - Taxes on Alcoholic Beverages*"). In *Japan - Alcohol*, the Appellate Body similarly upheld the Panel's analysis of the marketplace in its assessment of "directly competitive." The Appellate Body stated that "[t]his seems appropriate. The GATT 1994 is a commercial agreement, and the WTO is concerned, after all with markets. It does not seem inappropriate to look at competition in relevant markets as one among a number of means of identifying the broader category of products that might be described as 'directly competitive or substitutable." Report of the Appellate Body, *Japan - Alcohol*, at p. 25.

satisfying a particular need or taste, or, in markets where regulatory barriers exist, latent demand.[8]

7. The United States notes that the findings discussed above concern the phrase "directly competitive and substitutable" for purposes of the *Ad* Article III:2 of the GATT 1994. Because the Appellate Body did not divorce the phrase "directly competitive" from "substitutable", these findings should not be transferred in their entirety to cases involving Article 6 of the ATC, which refers only to "like and/or directly competitive products."[9] The Appellate Body's findings suggest that "directly competitive" reflects the actual state of affairs on the marketplace. By contrast, the Appellate Body relies on the term "substitutable" in its assessment of "potential" competition or "latent" demand.[10] In any case, the Panel should be cautious about imputing interpretations of the phrase "directly competitive or substitutable" to interpret the term "like and/or directly competitive."

8. Moreover, the Appellate Body's findings in *Korea - Taxes on Alcoholic Beverages* are not directly applicable to this case given that they are based on the object and purpose of Article III of the GATT, which is very different from that of Article 6 of the ATC.[11] As the Appellate Body explained, the objectives of Article III of the GATT are to avoid protectionism in the application of internal tax and regulatory measures, require equality of competitive conditions, and protect expectations of equal competitive relationships.[12] These objectives, though important, are not the objectives of Article 6 of the ATC. As the first sentence of Article 6.1 makes clear, the objective of Article 6 is to permit Members to apply a special transitional safeguard during the ten year transition to the rules of the GATT. The Panel should therefore be very cautious about relying on findings based on the object and purpose of Article III of the GATT to interpret the provisions of the ATC.

9. Nevertheless, as applied to facts of this case, the Appellate Body's findings on "directly competitive or substitutable" support the U.S. conclusion that combed cotton yarn manufactured

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[8] Report of the Appellate Body, *Korea - Taxes on Alcoholic Beverages*, at ¶ 114.

[9] "Directly competitive" and "substitutable" have distinct meanings. The *New Shorter Oxford English Dictionary* defines "competitive" as "of, pertaining to, involving, characterized by, or decided by competition" and defines "substitutable" as "able to be substituted."

[10] "In our view, the word 'substitutable' indicates that the requisite relationship *may* exist between products that are not, at a given moment, considered by consumers to be substitutes but which are, nonetheless, *capable* of being substituted for one another." Report of the Appellate Body, *Korea - Taxes on Alcoholic Beverages*, at ¶ 114.

[11] For a discussion of the object and purpose of the ATC, *see infra* Answer to Question 3 *and* first written submission of the United States, at ¶ 37-43.

[12] Based on these objectives, the Appellate Body declined to take a "static view" of "directly competitive or substitutable" which the Appellate Body explained "cannot be limited to situations where consumers already regard products as alternatives." Again relying on the word "substitutable", the Appellate Body stated, "If reliance could be placed only on current instances of *substitution*, the object and purpose of Article III:2 could be defeated..." Report of the Appellate Body, *Korea - Taxes on Alcoholic Beverages*, at ¶ 120. (emphasis supplied)

by vertically integrated fabric producers for internal consumption is not "directly competitive" with imports of combed cotton yarn. Combed cotton yarn manufactured for subsequent internal consumption does not enter the combed cotton yarn marketplace. As explained in the Market Statement, vertically integrated fabric producers attempt to balance their production as closely as possible at each stage of the production process[13] and therefore attempt to manufacture only as much combed cotton yarn as needed for their own internal consumption in the production of a subsequent fabric product.[14] Unlike combed cotton yarn for sale establishments – whose business is exclusively to spin yarn for weavers, knitters, and other manufacturers[15] – vertically integrated fabric producers would not take orders for yarn from customers, have a sales price for yarn, maintain sales inventory of yarn, or have a market share for yarn. Therefore, vertically integrated producers of fabric and other non-yarn products do not have actual or potential customers for combed cotton yarn on the marketplace.

10. Pakistan is unable to challenge this evidence and introduces speculation in an effort to confuse the issue. In its first written submission, Pakistan attempted to undermine the facts presented in the Market Statement by introducing hypothetical situations where combed cotton yarn manufactured by vertically integrated producers of non-yarn products *might theoretically* compete with imports of combed cotton yarn.[16] Pakistan has provided no evidentiary support for the speculation it introduces, and the United States was aware of no such circumstances at the time it prepared its Market Statement.[17] Therefore, the United States would urge the Panel to rely on the unrebutted facts of the case as presented in the Market Statement and refrain from engaging the speculation put forth by Pakistan.[18] Products that compete only in a non-market, theoretical, and speculative sense are not directly competitive based on the ordinary meaning of this term as considered in light of the object and purpose of Article 6.

11. Therefore, the Panel should give full meaning to the term "directly competitive" contained in Article 6.2 and should not – as Pakistan and India have suggested – read these words out of the ATC. The ordinary meaning of "directly competitive" read in light of the object and purpose of the ATC means that products are directly competitive only when the real facts of

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[13] Market Statement, at Appendix I.

[14] *See* first written submission of the United States, at ¶¶ 46-48 and notes 37 and 38.

[15] Phyllis G. Tortora and Robert S. Merkel, *Fairchild's Dictionary of Textiles*, (7th ed, 1996), p. 485. *See* First Submission of the United States, at ¶ 45.

[16] *See e.g.*, first written submission of Pakistan, at note 33.

[17] As the United States stated in the Market Statement, the "USG verified that less than five percent of the integrated sector's yarn consumption was purchased from the 'for sale' market during the period covered by the investigation." Market Statement, at Appendix I. Subsequent verification revealed that vertically integrated producers purchase roughly two percent of their consumption of combed cotton yarn from the market and sell roughly one percent of their production on the open market. First written submission of the United States, at ¶ 69.

[18] In *Korea - Taxes on Alcoholic Beverages*, the Appellate Body affirmed the Panel's conclusion that there was "'sufficient unrebutted evidence...to show *present* direct competition between the products'...this legal finding is...based firmly in the present." Report of the Appellate Body, *Korea - Taxes on Alcoholic Beverages*, at ¶ 113.

the case – firmly rooted in the present, *not* speculation – demonstrate that they compete with each other on the marketplace. In this case, the combed cotton yarn manufactured by vertically integrated establishments is consumed internally, is not intended for release onto the market, and thus does not compete with imports of combed cotton yarn on the marketplace. Therefore, such yarn is not a "directly competitive product" with imports of combed cotton yarn.

Question 2: *Do you consider the reference in the Antidumping Agreement to the "domestic industry as a whole" to be broader or narrower than the reference to the "domestic industry" in the ATC? With reference to Pakistan's first Submission, Pages 26-27, and the US First Submission, para 59, please elaborate more.*

12. The United States does not consider that "domestic industry as a whole" provision of the WTO Antidumping Agreement[19] is generically broader or narrower than the "domestic industry" provision contained in the ATC. What can be said is that the two provisions are different, both textually and in the context and purpose of the agreements that they serve. As the United States noted in its First Submission, the ATC provides no definition for domestic industry, but rather refers to "the domestic industry producing like and/or directly competitive products."[20] The Antidumping Agreement devotes an entire Article to the definition of "domestic industry," reflecting precise concepts agreed upon after many months of negotiations and years of collective experience in antidumping practice among the negotiating Members. Thus, the Antidumping Agreement defines the term "domestic industry," as "the domestic producers as a whole of the like product or . . . those of them whose collective output of the products constitutes a major proportion of the total domestic production of those products."[21] Further, the Antidumping Agreement provides for certain exceptions to the general definition, *i.e.,* Members may exclude producers who are related to importers from the industry, and may in certain circumstances define the domestic industry by region.[22]

13. The ATC and the Antidumping Agreement also used different concepts to identify the products produced by the "domestic industry." For the Antidumping Agreement, the products are "like products;" for the ATC, the products are "like and/or competitive products." The *New Shorter Oxford English Dictionary defines* "and/or" as "either together or as an alternative." The ordinary meaning of the textual language of the ATC then does not limit the domestic industry identification to producers of "like products," but also permits the "domestic industry" for purposes of Article 6 to be producers of "like and directly competitive" products or "like" or "directly competitive" products. It is noteworthy that the ATC draws from the phrase "like

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[19] *Agreement on the Implementation of Article VI of the General Agreement on Tariffs and Trade 1994* (the "Antidumping Agreement").

[20] First written submission of the United States, at ¶¶ 59-60.

[21] Antidumping Agreement, Art. 4.

[22] Antidumping Agreement, Art. 4.1 (i) and (ii).

and/or directly competitive products" from the MFA[23] rather than the definition of "domestic industry" from the Antidumping or any other WTO agreement.[24]

14. On the pages of Pakistan's submission to which the Panel cites, Pakistan appears to misunderstand the underpinnings of the Antidumping Agreement. Pakistan specifically states that "there is no reason why the issue of market segmentation in the case of safeguard action under Article 6 of the ATC...should be resolved differently than in the cases of...antidumping measures."[25] A *safeguard* action under Article 6 of the ATC is very different from *dumping* under Antidumping Agreement. Indeed, both Article VI of GATT 1994 and the Antidumping Agreement that implements that Article deal with dumping, *i.e.*, situations where a product is being introduced into the commerce of another country at less than fair value.[26] While Article VI of the GATT 1994 specifically *condemns* injurious dumping, the ATC authorizes transitional safeguard action that meet the terms of Article 6. Therefore, Pakistan's attempt to portray the U.S. decision concerning a transitional safeguard taken under the ATC as departing from past decisions under the Antidumping Agreement, or as potentially having a detrimental future impact on the application of the Antidumping Agreement, is misplaced at the outset.[27]

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[23] *See* MFA, Art.3 and Annex A. *See also infra* answer to question 4 for a discussion of the phrase "like and/or directly competitive" in the MFA,

[24] Some commentators have suggested that, when the ATC was being negotiated, the negotiators discussed adopting the definition of "domestic industry" used in antidumping agreements but rejected that notion. Marcelo Raffaelli and Tripti Jenkins, *Drafting History of the Agreement on Textiles and Clothing*, 1995, at 79 ("Raffaelli and Jenkins"). The ATC also did not draw from other non-transitional WTO agreements (such as Article XIX of the GATT) for purposes of the "domestic industry producing like and/or directly competitive products." First written submission of the United States, at ¶ 61.

[25] First written submission of Pakistan, at p. 26.

[26] Antidumping Agreement, Art. 2.1.

[27] Even if the Panel undertakes a factual comparison of antidumping cases and the instant action, Pakistan's arguments do not withstand scrutiny. In particular, Pakistan argues that U.S. action in this case was inconsistent with U.S. arguments in *Mexico - High-Fructose Corn Syrup*. As discussed in the first written submission of the United States, Mexico's failure to undertake an analysis of the entire industry it had identified in its antidumping analysis was precisely the error that formed the basis for the U.S. argument that Mexico "simply failed to address the question of the threat of injury to the industry it had defined as the relevant industry." Mexico had identified the domestic industry for purposes of its antidumping action to include production of all sugar. However, Mexico only analyzed the effects of the imports on *part* of that production by considering only sales to industry and excluding sales to household users. As a result, the data considered for purpose of the injury analysis did not reflect the industry as a whole. In this case, by contrast, the United States has considered the entire industry producing combed cotton yarn for sale in reaching its damage analysis, as it has identified it for purposes of the Article 6 analysis.

Question 3: *Please elaborate how the object and purpose of the ATC demands your interpretation on the scope of a subject domestic industry under Article 6 but rejects the other party's interpretation. Also, please elaborate further in what precise aspect the ATC is or is not special enough to demand a different interpretation of the term "directly competitive" from that of the comparable terms used in other WTO Agreements.*

15. The object and purpose of the ATC upholds the U.S. view that the phrase "domestic industry producing like and/or directly competitive products"permits the identification of the domestic industry on the basis of directly competitive products. This approach – built into the plain text of the term "like and/or directly competitive"[28] – is given full meaning when considered against the object and purpose of the ATC.

16. The ATC sets forth a careful balancing of interests between exporting and importing Members to guide the textiles and clothing sector through the delicate ten-year transition from a regime of special quotas to GATT rules.[29] For importing Members, a fundamental aspect of this bargain was the ability to address damaging surges in imports of non-integrated products through a special safeguard provision *separate from* Article XIX of GATT 1994 and the WTO *Agreement on Safeguards* ("Safeguards Agreement"). Article 6.1 specifically recognizes that "during the transition period it may be necessary to apply a specific transitional safeguard mechanism." Once that transition is over and textiles and clothing products have been integrated into the GATT, the special, transitional safeguard provision will no longer be available, and textile and clothing products will fall under the normal safeguard rules of the GATT and the Safeguards Agreement. These objectives demand an interpretation of Article 6 that will permit Members to utilize the transitional safeguard mechanism to address a damaging surge in imports.

17. Article 6.2 permits Members to define the domestic industry in a manner that reflects the marketplace. The list of factors set out in Articles 6.2 and 6.3 for the assessment of serious damage/actual threat thereof emphasizes this emphasis on the market. Transitional safeguard action can only be established after a consideration of a series of market-based economic variables – including output, productivity, utilization of capacity, inventories, market share, exports, wages, employment, domestic prices, profits, investment, and consumer preferences. These variables are only relevant to domestic industries producing goods on the marketplace in direct competition with imports. It would not be feasible to obtain information for many of these factors for goods that do not compete on the marketplace, and in turn, to give meaning to the requirements set out in Articles 6.2 and 6.3.[30]

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[28] For a discussion of the ordinary meaning of the phrase "like and/or directly competitive products," *see infra* answer to Question 15.

[29] Article 1.1 of the ATC states "This Agreement sets out provisions to be applied by Members during a transition period for the integration of the textiles and clothing sector into GATT 1994."

[30] Applied to the facts of this case, vertically integrated fabric producers do not sell combed cotton yarn that they consume on the market and do not directly compete with imports; therefore many of these factors are not relevant for the yarn they manufacture. Vertically integrated fabric producers would not have market share, exports,

18. Pakistan wrongly believes that the mere manufacture of a physically like article – even if it is not released onto the market and even if it does not directly compete with the import in question – should determine the scope of a domestic industry for purposes of the ATC.[31] This interpretation denies the relevance of the marketplace for purposes of transitional safeguard action. Under Pakistan's approach, it would be infeasible for a Member to analyze many of the market based factors listed in Article 6.2 and 6.3 and therefore impossible to resort to the Article 6 transitional safeguard mechanism. This interpretation would render Article 6 ineffective and would be contrary to the object and purpose of Article 6.

19. Essentially, Pakistan is asking the Panel to read the words "directly competitive" out of the ATC and to require an interpretation of the "domestic industry producing like and/or directly competitive products" to include establishments manufacturing goods that do not enter the market, do not compete with imports, are not directly affected by imports, and would not suffer serious damage or actual threat of serious damage during an import surge. That was not part of the carefully negotiated balance struck by the ATC.

20. Lastly, the Panel has asked the Parties to elaborate further on which aspect of the ATC is special enough to demand a different interpretation of the term "directly competitive" from that of comparable terms used in other WTO agreements. As the United States explained in its introductory remarks, the United States believes that the Panel must analyze the meaning of the term "directly competitive" within the "four corners of the ATC" based on the facts of this case and considered in light of the object and purpose of Article 6 and the ATC.

21. Given that the ordinary, dictionary meaning of the term "directly competitive" may be no different between agreements, it is the context and the unique object and intent of the ATC that gives special meaning to "directly competitive" for purposes of Article 6. As the United States has discussed, the text, object, and purpose of Article 6 is special and unique and is entirely different from that of non-transitional agreements. Unlike *Ad* Article III:2 of the GATT, Article XIX of the GATT, the Antidumping Agreement and the Safeguards Agreement, Article 6 uses the special term "like and/or directly competitive," which derives from the MFA and not any WTO agreement. Unlike these other provisions, Article 6 of the ATC establishes a special transitional safeguard for textile and clothing items not yet integrated into the GATT, while

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prices or profits for combed cotton yarn. Moreover, there is no evidence that vertically integrated fabric producers separately track inventories, productivity, wages, employment, or investment with respect to combed cotton yarn; instead, they would consider these factors solely for purposes of their fabric production. And because they do not manufacture combed cotton yarn with an intent to sell it, changes in consumer preferences would not affect their decisions. It would thus be impractical for a Member to obtain much of the information required under Article 6.2 and 6.3 with respect to combed cotton yarn spun by vertically integrated fabric producers.

[31] According to Pakistan, because combed cotton yarn manufactured by vertically integrated establishments is "like" imports of combed cotton yarn, the "question of whether the yarn produced by vertically integrated mills is directly competitive is consequently irrelevant." Statement of Pakistan at the First Meeting of the Panel, at p. 5.

Article XIX of the GATT and the Safeguards Agreement govern safeguard actions for items already integrated into the GATT. Unlike the non-transitional agreements, the ATC covers a sector that has historically been outside the normal trading rules and is designed to integrate that sector into the normal rules of the GATT over a ten-year period in the least disruptive manner possible.

22. Accordingly, the four corners of the ATC – which include its unique text, its unique context, and its unique purpose – provide sufficient guidance for the Panel to determine the scope of "directly competitive" for purposes of the facts posed by this case. It would be unnecessary and inappropriate for the Panel to look elsewhere.

Question 4: *With respect to the MFA,*

> *(a) What is your interpretation of "like and/or directly competitive products" under Annex A to the MFA (please provide any supporting documents)?*

23. Under the MFA, the phrase "like and/or directly competitive products" defined the market for purposes of "market disruption," or safeguard, actions under that agreement. Annex A, in which this term appears, contained the specific definition of the factors to be evaluated in taking safeguard actions under Article 3 of the MFA. Article 3.2 and 3.3 of the MFA read (in relevant part):

> "2. The participating countries agree that this Article should only be resorted to sparingly and its application shall be limited to the precise products and to countries whose exports of such products are causing market disruption as defined in Annex A. ..."
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> "3. If, *in the opinion of any participating importing country, its market* in terms of the definition of market disruption in Annex A *is being disrupted* by imports ....." (emphasis supplied)

Annex A to the MFA, paragraph I, reads as follows:

> I. The determination of a situation of "market disruption", as referred to in this Arrangement, shall be based on existence of serious damage to domestic producers or actual threat thereof. Such damage must demonstrably be caused by the factors set out in paragraph II below and not by factors such as technological changes or changes in consumer preference which are instrumental in switches to like and/or directly competitive products made by the same industry, or similar factors. The existence of damage shall be determined on the basis of an examination of the appropriate factors having a bearing on the evolution of the state of the industry in question such as: turnover, market share, profits, export

performance, employment, volume of disruptive and other imports, production, utilization of capacity, productivity and investments. No one or several of these factors can necessarily give decisive guidance.

24. Read together, Article 3 and Annex A clearly embodied two specific and relevant concepts. First, the market disruption provision of the MFA begins with the domestic market and requires an analysis of the impact of imports of like and/or directly competitive products *on the domestic marketplace*. Annex A focuses on "market disruption" as evidenced by serious damage to domestic producers. Second, Article 3 makes it clear that the importing country had the ability to determine, in its opinion, whether market disruption had occurred, within the definition of Annex A.

25. Probably the most prominent example of agreement among MFA signatories on the term "like and/or directly competitive" is found in paragraph 24 of the 1986 Protocol of Extension of the MFA, which expanded the MFA's fiber coverage from cotton, wool and man-made fiber textiles and textile products to include silk blend and non-cotton vegetable fibers (such as ramie), and blends thereof.[32] In paragraph 24, MFA signatories underscored the importance and meaning of the term *directly competitive* for purposes of the MFA's safeguard provision.[33] By agreeing to expanded fiber coverage, MFA signatories explicitly acknowledged that textile products made from the so-called "new MFA fibers," while perhaps not identical to textile products made from traditional MFA fibers, nonetheless were *directly competitive* on the market.[34] Therefore, the United States believes that the Panel should note the relevance of the term "directly competitive" to the market disruption provision of the MFA in conducting its assessment of this term under Article 6 of the ATC.

(b) To what extent is this relevant to the interpretation of "like and/or directly competitive products" under Article 6 of the ATC?

26. The MFA is relevant as providing context for the interpretation of "like and/or directly competitive products" for purposes of Article 6. The Appellate Body was very clear in *United States - Underwear* that the "prior existence and demise, as it were, of the MFA" informs the context of Article 6 of the ATC.[35] In that case, the Appellate Body drew strong inferences from

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[32] This paragraph is attached as U.S. Exhibit 10 ("U.S.-10").

[33] "Accordingly, the Committee agreed that the provisions of Articles 3 and 4 may be invoked with respect to directly competitive imports of such textiles..." 1986 Protocol Extending the MFA, ¶ 24 (i).

[34] A U.S. observer noted, "...few looking at a ramie sweater and an identically styled sweater made of a cotton-blend could seriously contend that the products were not directly competitive." Brenda A. Jacobs, *Renewal and Expansion of the Multifiber Arrangement, Law & Policy in International Business*, Volume 19, 1987, p. 42.

[35] Report of the Appellate Body, *United States - Underwear*, at p. 16. In this regard, the Appellate Body noted that "[w]ith the demise of the *MFA*, its place has been taken...firstly, in respect of textile and clothing items not yet integrated into the *General Agreement*, by the *ATC*. Secondly, in respect of items already integrated into the

the disappearance of certain MFA language in the text of the ATC.[36] Likewise, in this case, the Panel should draw strong inferences from the fact that the ATC retains the MFA phrase "like and/or directly competitive products" and does not draw from GATT Article XIX or other non-transitional WTO agreements. In addition, as relevant context, U.S. market disruption analyses and safeguard actions taken on yarn products under the MFA were based on an examination of the yarn for sale industry, rather than the industry producing fabric, apparel, or home furnishings in a vertically integrated facility, which also manufactured combed cotton yarn for its own consumption in the production of these other end products.

27. In this regard, Rafaelli and Jenkins explain that "[o]ne must acknowledge ... that the MFA was very present in the minds of the authors of the ATC, that the ATC incorporates several concepts and much language taken from the MFA, and that its negotiation was influenced by precedents established and by facts which occurred in the course of the MFA's life."[37] This is particularly so for Article 6: "[i]n the MFA, on which so much of the language of Article 6 of the ATC was based...[38].

28. The interpretation given to "like and/or directly competitive" as products which compete on and impact on *the marketplace*, and the U.S. practice with respect to the yarn industry in the context of MFA safeguards should inform an interpretation of Article 6, which drew heavily from the MFA. Indeed, the MFA's focus on the marketplace and direct competition provide appropriate and reasonable context for interpreting Article 6 of the ATC based on the facts and circumstances of this case.

Question 5: *Pakistan's First Submission, footnote 33 and US First Submission, para. 46 are in disagreement as to whether imports of combed cotton yarn can cause "damage" to producers of that product for their own use. Please further elaborate on this point. In this connection, please discuss whether the subject transitional safeguard measure helps protect those producers from competition with combed cotton yarn imported from Pakistan. If so, how? If not, what are the characteristics of the market that isolates them from the effect of such protection?*

29. The United States notes, as an initial matter, footnote 33 of Pakistan's First Submission and paragraph 46 of the U.S. First Submission are entirely different in character. Pakistan's footnote 33 relies on supposition and speculation. By contrast, the information contained in paragraph 46 of the U.S. First Submission reflects verified facts and U.S. findings based on these facts. Therefore, the United States believes that the Panel should grant little weight to the

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General Agreement, the *MFA* safeguard measure is displaced by Article XIX of the *General Agreement* and the *Agreement on Safeguards*." Report of the Appellate Body, *United States - Underwear*, at p. 16, note 26.

[36] Report of the Appellate Body, *United States - Underwear*, at p. 17.

[37] Rafaelli and Jenkins, p. 88.

[38] Rafaelli and Jenkins, p. 110.

conjecture expressed in footnote 33 as compared to the actual situation in the U.S. domestic industry at the time of the investigation that served as the basis for the Market Statement and the transitional safeguard action.

30. Vertically integrated producers of fabric do not normally enter the marketplace for yarn, either as a buyer or seller. Their combed cotton yarn output is not intended to enter the market to compete with imports.[39] Therefore, under the facts of this case, neither the increase of combed cotton yarn imports nor the subject transitional safeguard measure is of immediate relevance to vertically integrated fabric, apparel, or home furnishings producers.

31. In footnote 33, Pakistan suggests that lower cost imports from Pakistan may eventually impact vertically integrated mills. In Pakistan's view, "if yarn is available on the merchant market at a cost lower than the cost of producing yarn internally, a vertically integrated facility will normally cease yarn production and turn to the merchant market instead."[40]

32. Pakistan's view that vertically integrated facilities would completely restructure simply to take advantage of low cost imports is based on an overly simplistic view of the initial business decision that led these establishments to vertically integrate. An establishment that is structured to make its production of fabric independent of the "for sale" market achieves advantages other than merely being in a position to produce low-cost yarn. Vertical integration as to yarn allows fabric producers to control the quality, type, delivery, and supply of the yarn that serves as input to their fabric in ways that would not be available if the fabric producers were dependent on external supplies. Vertical integration can lead to predictability and efficiencies that, from a business perspective, justify continued vertical integration even if yarn in the market is being sold at very low prices.

33. Nevertheless, it is possible that the 283.2 percent increase in imports of low cost combed cotton yarn from Pakistan could eventually have an indirect effect on vertically integrated producers of fabric. It is also possible that this import surge could eventually have indirect effects on other industries and business in the United States, including cotton growers, electrical utilities, regional banks, lawyers, pension funds, and indeed, Pakistan's shipments may eventually break apart the very structure of the sales yarn industry versus the vertically integrated industry making fabric, apparel, or home furnishings with their own yarn. Of course, at the time of the Market Statement, vertically integrated producers were not part of the combed cotton yarn industry, and this fact, not Pakistan's speculation, is what is relevant.

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[39] The sales yarn and the vertically integrated fabric, apparel, or home furnishing industries in the United States have had, since statistics started to be collected in 1959, and continuing to this day, separate, distinct identities and characteristics. The term "sale yarn" or "sales yarn" has been a commonly understood industry definition for many decades. As the United States discussed in the Market Statement, the U.S. investigation focused on the sales yarn industry, since only the output of the sales yarn industry enters the yarn marketplace in competition with imports. Market Statement, at ¶ 3.1.

[40] First written submission of Pakistan, at 25, note 33.

34. The effect of the transitional safeguard on vertically integrated producers of fabric is indirect just as its impact on cotton growers and other industries is indirect. Given that vertically integrated facilities producing fabric, apparel or home furnishings from their own yarn do not normally enter the market for yarn and are not part of the relevant domestic industry, the transitional safeguard measure does not necessarily protect, nor does it harm, their economic interests. The effect, if any, might differ based on the markets, production methods, capital equipment, and other business considerations involved.

35. Therefore, the effect of either increased combed cotton yarn imports or the subject transitional safeguard on vertically integrated producers of fabric, apparel, or home furnishings is, at best, indirect. Nothing in the ATC requires a Member to consider these indirect effects.

Question 6: *In discussing the treatment of those plants retooled to produce carded cotton yarn or other products than combed cotton yarn, please compare the interpretation of the term "serious damage" under Article 6.2 and that of "serious injury" contained in the Safeguards Agreement.*

36. "Serious damage" and "serious injury" are different terms that must be interpreted in light of their context. Article 4.1 of the Safeguards Agreement defines "serious injury" as "a significant overall impairment in the position of a domestic industry." Unlike the Safeguards Agreement, the ATC does not define "serious damage" or otherwise establish any standard for what is to be considered "serious damage." Rather, the ATC places in the hands of the importing Member the responsibility for determining whether a particular product is being imported in such increased quantities as to cause serious damage or actual threat thereof, without providing any guidance as to what serious damage might be.

37. Specifically, Article 6.2 provides that "safeguard action may be taken under this Article when, *on the basis of a determination by a Member*, it is demonstrated that a particular product is being imported into its territory in such increased quantities as to cause serious damage or actual threat thereof..." While the ATC does list factors to be considered by a Member in assessing whether serious damage has occurred, it does not set the parameters for what is to be considered serious damage that would guide a Member's determination. Thus, it is for Members, after considering the factors set forth in Article 6, to define serious damage in the context of a particular safeguard investigation.

38. The context of Article 6 is relevant. With the "demise" of the MFA, its safeguard provision was replaced by Article 6 of the ATC for non-integrated textile and clothing products and by Article XIX of the GATT and the Safeguards Agreement for integrated textile and clothing products.[41] In other words, although the term "serious injury" of Article XIX of the

[41] Report of the Appellate Body, *United States - Underwear*, at p. 16 and note 26.

GATT was available at the time the ATC was drafted, that phrase was chosen only to apply to integrated textile and clothing products, *not* to non-integrated textile and clothing products. Instead, the ATC uses the term "serious damage"– a term that drew from the MFA and did not carry with it the connotations that might attach to "serious injury."[42] In the U.S. view, the use of "serious damage" rather than the terminology contained in either Article XIX or Article VI of the GATT strongly supports the argument that the bargain struck in the ATC was special and unique and that the language of the ATC must be interpreted on its own terms and not by reference to interpretations of Article XIX of the GATT, the Safeguards Agreement, or other non-transitional agreements.

39. However, putting that issue aside as the Panel has directed, one conclusion is inescapable regarding the choice of the term "serious damage" over "serious injury": "serious damage" does not, as Pakistan suggests, set a higher bar than "serious injury."[43] To suggest, as Pakistan does, that the ATC imposes a higher bar on the invocation of its transitional safeguard than is present in the Safeguards Agreement is to disregard the very purpose of the ATC. The purpose of the transitional safeguard in the ATC was not to make safeguard actions *more difficult* during the transitional period. The ATC itself was designed to ease the transition from the MFA to normal GATT rules over a defined period. Thus, the ATC's "specific transitional safeguard mechanism" could not have been designed to impose a more stringent damage test before its transitional safeguard could be invoked. To suggest that it does runs counter to the entire purpose and intent of the ATC. The context of the phrase "serious damage" – derived from the MFA – implies that "serious damage" was intended to give Members greater ability to address domestic market disruptions from floods of imports than was available under the Safeguards Agreement.

40. In any event, under an analysis of either term, the evidence that establishments were exiting the defined industry (e.g., *combed* cotton yarn) and undertaking the production of *other* products not within the defined industry (e.g., *carded* cotton yarn) is an important factor in the assessment of "serious damage" or a "serious injury." Of course, such evidence alone would not be dispositive of whether serious damage or injury to the defined industry had occurred. In both the Safeguards Agreement and the ATC, a Member is required to consider a number of other factors before reaching its determination of serious damage or serious injury. However, it is

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[42] Rafaelli and Jenkins, at 108-109. It should be noted that apparently the negotiators were also aware of the different language in the antidumping provision of Article VI of the GATT 1947 and chose not to use the language "material injury" either.

[43] On page 33 of its first written submission, Pakistan suggests that "serious damage" means "*grave* injury impairing value or usefulness." (emphasis supplied) "Grave" is defined by *Merriam-Webster's Collegiate Dictionary* as "significantly serious" and by *The New Shorter Oxford English Dictionary* as "of a matter: weighty, significant; requiring serious consideration...of a fault, difficulty, responsibility: highly serious, formidable." In other words, the ordinary meaning of "grave injury" appears to be something greater than "serious injury." Moreover, under the Article 4.1 of Safeguards Agreement, "serious injury" means "significant overall impairment in the position of the domestic industry." It is inexplicable why Pakistan suggests that pairing "serious" with "damage," as opposed to "injury," transforms the meaning from "significant" to "grave."

plain that, under both Agreements, evidence regarding the closure of firms within the defined industry is properly considered in a damage or injury investigation.

Question 7: *How difficult (technically or financially) is it to switch a plant producing combed cotton yarn into that producing carded cotton yarn? What measures (e.g. investments, replacement of machines, training of employees) are necessary to successfully convert a plant that produces combed cotton yarn into a plant that produces carded cotton yarn?*

41. "Combing" is a necessary step in the production of combed cotton yarn. The combing process relies on high grades of cotton, requires specialized machinery, and produces a product which is intended for specified, distinct market niches (i.e., higher quality).

42. *Fairchilds's Dictionary of Textiles* defines "combing" as a step that is subsequent to the carding process in yarn manufacture.[44] In the cotton spinning system, "combing" is used to produce finer, smoother cotton yarns than merely carding. The combing process physically separates the long, choice, desirable fibers from knots, impurities and shorter, weaker fibers in the cotton before it is spun. As a result of the combing process, the combed cotton yarn produced is finer, cleaner, more lustrous, and stronger than carded cotton yarns. By contrast, carded yarn contains a wider range of fiber lengths and, as a result, are not as uniform or as strong as combed yarns.

43. Only better grades of cotton may be combed. Purchases of these better grades of cotton are contracted for, usually in advance of the new harvest for these fibers, at premium prices, 15 percent (or more) above prices for cotton grades that are used for carding.

44. The domestic market in the United States for carded cotton yarn is roughly five times larger than the domestic market for combed cotton yarns.[45] *Carded* cotton yarns are generally used in coarser, heavier-weight fabrics (such as denim, canvas, osnaburg, blanketing and heavy knitwear such as sweaters, tube socks, or fleece). *Combed* cotton yarns are generally used in thinner, lighter-weight, higher quality fabrics (such as fine gauge jersey knits, broadcloth, percale or lawn/batiste).

45. As explained by the United States in its first written submission, "Pakistan overstates the ease with which a plant can convert production from combed cotton yarn to carded cotton yarn.

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[44] The production of combed cotton yarn involves nine separate steps: (1) opening and blending of fibers, (2) carding/sliver, (3) breaker drawing, (4) lap winding, (5) combing/sliver, (6) finishing drawing, (7) roving, (8) spinning, and (9) winding. Combed cotton yarn for sale then is sold to the customer. Combed cotton yarn for internal consumption is then made into fabric.

[45] Office of Textiles and Apparel, United States Department of Commerce, *U.S. Imports, Production, Markets, Import to Production Ratios and Domestic Market Shares for Textile and Apparel Product Categories*, May 2000, at p. 6.

Pakistan fails to take into account the amortization cost of idling equipment, lost plant and equipment facility, and marketing cost required to establish a new customer base. Because of the financial risk involved, such conversions are generally not feasible without a substantial re-engineering of the facility."[46]

46. Specifically, conversion of a plant from the production of combed cotton yarn to the production of carded cotton yarn would engender the following serious financial and technical obstacles:

- the plant would have incurred higher raw material costs for premium grade cotton, contracted in advance of the new harvest for these fibers, at the same time as the output of the plant was reduced in value;

- the plant would bear the amortization and opportunity costs of idling of expensive additional equipment required for combing operations. (In addition, fixed costs for building, air conditioning, warehouse, office space, and auxiliary service equipment would continue to accrue.);

- in the absence of the combing operations, more of the cotton fiber would be available to be spun. Since the installed spindles are "balanced" (that is, from the opening of the raw cotton fiber to the packaging of the spun yarn) for the smaller quantity of raw materials that would result from a combing process, the plant would need to either install new spindle capacity to pick up the additional cotton fiber, or idle some of the preparatory machinery, increasing costs in either circumstance;

- the plant may require new construction in order to maintain operating efficiencies;

- idled equipment would result in the elimination of production worker jobs; and

- finally, the plant would need to invest in research and marketing efforts to develop a new customer base in a larger market than combed cotton yarn subject to greater competitive pressures.

47. The conversion from combed to carded yarn offers no assurance of success in the carded yarn market. As the United States noted in its first written submission, one of the three establishments producing combed cotton yarn during the period covered by the U.S. investigation into serious damage and actual threat thereof, China Grove Textiles, attempted the conversion of a plant from combed cotton yarn to carded cotton yarn. The plant was not competitive in the carded yarn market and was closed. The experience of China Grove Textiles exemplifies the

[46] First written submission of the United States, at note 133.

point that the attempted conversion from a combed yarn mill to a carded yarn mill is a complicated, expensive and uncertain endeavor, not undertaken lightly or routinely.

Question 8: *Before the investigation period, were there other cases of producers leaving the combed cotton yarn industry (including all segments; see para. 4.1 of the Market Statement) for restructuring or modernization, say, in the preceding 5 years? Please identify the reasons for the producers leaving the industry. How does the leaving of producers equate with the on-going process of "autonomous industrial adjustment" as referred to in Article 1.5 of the ATC?*

48. For purposes of the Market Statement, the United States did not investigate whether producers had exited the combed cotton yarn industry during the previous five-year period. Rather, consistent with the terms of Article 6.7 of the ATC, the United States considered evidence of plant closures during the two year and eight month period of its investigation of serious damage and actual threat thereof. Article 6.7 requires that information with respect to the factors in Article 6.3 be "as up to date as possible" and related as closely as possible to the 12-month reference period set out in Article 6.8. The United States considered the information on plant closures to be relevant in the context of Article 6.3, and therefore included in the Market Statement the information that three mills which produced combed cotton yarn for sale which had exited the industry during the period 1996, 1997 and January-August 1997/1998.

49. Given the requirements of Articles 6.7 and 6.8, the United States did not examine whether additional mills had exited the combed cotton yarn business in the five years prior to the period of investigation. Nevertheless, the United States was aware that additional mills producing combed cotton yarn exited the industry in the lead up to the period of investigation. However, the United States chose to limit its analysis of firms exiting the industry to the period of investigation and, accordingly, did not consider these developments in its determination of serious damage/actual threat thereof.

50. Furthermore, given that the U.S. investigation focused on the sales yarn industry, the United States focused on vertically integrated fabric producers only to establish that these mills purchase and sell *de minimis* amounts of combed cotton yarn. The United States did not specifically investigate whether these vertically integrated mills stopped manufacturing combed cotton yarn.

51. As the United States explained in its first written submission, the United States considered the evidence of three mills exiting the combed cotton yarn for sale industry as one of the many factors that the United States examined in its assessment of serious damage.[47]

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[47] First written submission of the United States, at ¶ 168. The United States based its determination on a wide-range of additional factors, including production, shipments, exports, capacity utilization, inventories, unfilled orders, wages, productivity, profits, investment, market share, import share, prices, and the apparent domestic market.

Evidence of mills leaving the industry may also indicate that the industry was also undergoing the process of "continuous autonomous industrial adjustment" referred to in Article 1.5 of the ATC. However, these two concepts – "serious damage" and "continuous autonomous industrial adjustment" – are not, as Pakistan suggests,[48] mutually exclusive. An industry may suffer serious damage or actual threat of serious damage *at the same time* that it is in the process of readjusting or retooling. The ATC explicitly recognizes this fact by providing a transitional safeguard mechanism *during* the ten-year restructuring period given to the textiles and clothing sector. Far from being incompatible with continuous autonomous adjustment, as Pakistan suggests, the Article 6 safeguard is an essential element in this restructuring process. Article 6 gives industries seriously damaged by increased imports the ability to adjust.

52. As the United States explained in its first written submission, the case before the Panel is one of forced restructuring which occurred as the direct result of serious damage to the industry caused by a surge in imports.[49] The fact that some mills went on to restructure and retool should in no way minimize the serious damage facing the combed cotton yarn industry when the United States issued its Market Statement in December 1998. The facts and circumstances discussed in the Market Statement – including the number of mills exiting the industry and all other factors listed in Article 6.3 – clearly revealed a domestic industry suffering from serious damage and actual threat of serious damage.

Question 9: *Bearing in mind that serious damage or the threat of serious damage is caused by "increased quantities in total imports" (Art. 6.2), what precautions, if any, should be taken under the ATC in order to assure a transparent and equitable attribution of "serious damage" or "actual threat thereof" to a Member or Members? (For the United States) In the present case, how was it established whether combed cotton yarn from other sources than Pakistan did not contribute in a material way to the serious damage or threat thereof? What, precisely, was the basis of the differentiation of effects?*

53. Attribution under the ATC is unique in that Article 6.4 of the ATC authorizes application of a safeguard measure on a Member-by-Member basis. Article 6 itself contains provisions that ensure transparent and equitable attribution of serious damage and actual threat of serious damage based on the facts and circumstances of the case. By ensuring compliance with these provisions, the Panel will take the necessary precautions to ensure that the bilateral safeguard was appropriately invoked.

54. For example, Article 6.4 assures the appropriate and equitable attribution of serious damage and actual threat of serious damage. Under Article 6.4, attribution "shall be determined on the basis of a sharp and substantial increase in imports, actual or imminent, from such a Member or Members individually, and on the basis of the level of imports as compared with

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[48] First written submission of Pakistan, at p. 34.

[49] First written submission of the United States, at ¶ 167.

imports from other sources, market share, and import and domestic prices at a comparable stage of commercial transaction." While Article 6.4 notes that none of these factors, alone or in combination, can give definitive guidance, all of these factors must be carefully considered.

55. Moreover, Article 6.7 ensures that the information on which a safeguard action is based is transparent. Article 6.7 provides that the Member seeking to invoke a safeguard must provide the Member or Members who would be affected by the safeguard with "specific and relevant factual information, as up to date as possible, particular in regard to...the factors referred to in paragraph 4, on the basis of which it proposes to invoke the safeguard action with respect to the Member or Members." Article 6.7 assures that the Member who would be affected by the safeguard action has full access to the basis for that action. Moreover, the ATC also requires consultations between the Member proposing the safeguard and the Member or Members who would be affected by the safeguard.

56. The Panel has asked the United States to explain how it established whether combed cotton yarn from other sources than Pakistan did not contribute in a material way to the serious damage or threat thereof and what, precisely, was the basis of the determination of effect. In attributing serious damage to Pakistan, the United States strictly adhered to the provisions of Article 6.4. The United States examined the level of Category 301 imports from Pakistan as compared with imports from 29 other sources.[50] However, this factor (i.e., Pakistan imports compared to imports from other sources) is *only one* factor that Article 6.4 required the Member proposing the safeguard to consider in attributing serious damage to a Member or Members. Under Article 6.4, those other factors – considered together with a comparison of imports from other sources – must be the basis for the determination to attribute serious damage to a Member or Members. In this case, those other factors included the substantially lower price of Pakistan's Category 301 imports ($3.63 per kilogram) which were 26.2 percent below domestic prices ($4.92 per kilogram) and 20 percent below average world prices ($4.54 per kilogram). Indeed, as explained in the Market Statement, the extremely low price of Pakistan's imports exacerbated the impact of their surge.[51]

57. The Panel asks how the United States determined that imports from other sources did not "contribute in a material way" to the serious damage or actual threat thereof found to exist under Article 6.2. In contrast to Article 6.2 (which requires a demonstration that increased quantities of imports caused serious damage or actual threat thereof), Article 6.4 is not framed in terms of cause or contributing to the serious damage. Table V of the Market Statement demonstrates that there are numerous countries exporting Category 301 yarn to the United States. To some extent,

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[50] Market Statement, at Table V. Based on year-ending October 1998 data, the Market Statement established that Category 301 imports from Pakistan increased by 167 percent, world imports increased 68.9 percent, and imports from FTA countries (including Canada, Mexico, and Israel) increased 186.47 percent.

[51] See *infra* answer to Question 19 for the information the United States provided during the TMB review regarding the import price of Category 301 yarn from Mexico.

each of these countries "contributes in a material way" to the total increase in imports and thus to the serious damage caused by those increased imports.

58. However, *contribution* is not of significance for purposes of the Article 6.4 *attribution*. The question in an Article 6.4 analysis really is this: of the number of countries whose imports are a part of the total increase of imports that are causing serious damage, which is the Member or Members to whom this serious damage may be assigned? What is relevant for purposes of that analysis is the factors listed in Article 6.4: a sharp and substantial increase in imports, actual or imminent, and the level of imports as compared with imports from other sources, market share, and import and domestic prices at a comparable stage of production. Article 6.4 defines what must be considered in attributing serious damage and actual threat thereof. Any requirement that an importing Member must go beyond this would be inconsistent with the carefully negotiated balance of the ATC.

59. In this case, the United States carefully considered all these factors – including the increase in imports from other sources – in its Article 6.4 attribution analysis. The United States concluded that – even though imports from other sources were also increasing – serious damage or actual threat of serious damage was attributable to the 283.2 percent surge in imports from Pakistan. Pakistan's sharp and substantial surge in imports, together with the fact that its imports were priced so much lower that the average world price and the price of any FTA country made attribution to Pakistan appropriate under the terms of the ATC.

Question 10: *Please discuss whether Article 6.4 of the ATC, as a general matter, gives an importing Member the discretion to take a transitional safeguard measure against an exporting Member to whom serious damage is attributable, but simultaneously not to take such measure against another exporting Member whose exports are contributing to the same serious damage?*

60. As a general matter, the ATC contemplates that Members will establish a transitional safeguard actions only on those Members to whom the safeguard action can be attributed under strict terms Article 6.4 and not on all Members whose "exports are contributing to the same serious damage." As explained *supra* in the answer to Question 9, to some extent, each country contributing to the total imports causing the serious damage or actual threat thereof is contributing to that same serious damage. In the present case, each of the 29 sources listed in Table V contributed to some greater or lesser degree to the serious damage or actual threat thereof. The attribution analysis does not focus on cause as such, but rather on the Member or Members to whom the serious damage may be attributed according to the factors in Article 6.4. In short, Article 6.4 of the ATC gives an importing Member the discretion to take a transitional safeguard measure against an exporting Member to whom serious damage is attributable, but simultaneously not to take such measure against another exporting Member whose exports are contributing to the same serious damage.

Question 11: *Footnote 6 to Article 6.4 of the ATC states that it is not sufficient to examine just the existence of production capacity in exporting Members to determine whether increase in imports are imminent. Does this imply that such an examination of production capacity is at least required for analysis of actual threat of serious damage?*

61. The United States reads Footnote 6 to Article 6.4 more narrowly than the Panel's question suggests. Footnote 6 appears to relate to situations when attribution of serious damage/actual threat thereof is made on the basis of an *imminent*, rather than an *actual*, increase in imports.

62. Footnote 6 provides that "[s]uch an *imminent* increase shall be a measurable one and shall not be determined to exist on the basis of allegation, conjecture or mere possibility arising, for example, from the existence of production capacity in the exporting Members." (emphasis supplied) Footnote 6 elaborates on the word "imminent" in the Article 6.4:

> The Member or Members to whom serious damage, or actual threat thereof, referred to in paragraphs 2 and 3, is attributed, shall be determined on the basis of a sharp and substantial increase in imports, actual or imminent, from such a Member or Members individually and on the basis of the level of imports as compared with imports from other sources, market share, and import and domestic prices at a comparable stage of commercial transaction; none of these factors, either alone or combined with other factors, can necessarily give decisive guidance.

63. For example, Footnote 6 would appear to permit an Article 6 action if a Member attributing serious damage or actual threat thereof to another Member on the basis of specific information concerning goods "on the water," or otherwise in transit, which have not yet been imported. However, in this particular situation, the United States based its attribution of serious damage/actual threat thereof to the domestic industry producing combed cotton yarn for sale on an *actual* increase in imports of category 301 products from Pakistan, within the meaning of Article 6.4. As shown in the Market Statement, imports of combed cotton yarn from Pakistan registered an *actual increase of 283.2 percent* in the period January - August 1998 as compared to the January - August 1997 period.

64. The United States would like to point out that it could have, but did not under this more conservative reading of Footnote 6, consider production capacity statistics available to it at the time that it prepared the Market Statement. These statistics revealed that Pakistan's production capacity far outstripped that of other exporters.[52] Furthermore, as noted in the first written

[52] Statistics published by the International Textile Manufacturers Federation reveal that in 1996, Pakistan had installed capacity of 8.2 million short staple ring spindles. Short staple ring spindles are used in the production of combed cotton yarn, as well as other types of spun yarn. Pakistan's installed short staple capacity was greater than the countries of Western Europe combined, more than double the installed capacity of Mexico (with 3.5 million short staple ring spindles), and more than one-third higher than the installed capacity of the United States (with 4.9 million

submission of the United States, imports of Category 301 yarn from Pakistan have a history of high month-to-month volatility, demonstrating that Pakistan unquestionably has the capacity to surge dramatically in a short period of time. Since 1996, monthly imports from Pakistan have ranged from zero to over one million kilograms.[53]

Question 12: *What precisely are the parameters of a "prospective analysis" required to determine whether there is an actual threat of serious damage?*

65. Article 6 of the ATC sets forth no specific requirement regarding whether an importer must conduct a separate analysis of actual threat of serious damage and, if so, what the parameters of that analysis should be. It is not even clear whether, as this Question suggests, Article 6 requires a "prospective analysis" in assessing actual threat of serious damage. As the United States discussed in its first written submission, the text of Article 6 provides no separate definition or factors to distinguish "serious damage" from "actual threat of serious damage," and the overall purpose and context of Article 6 does not appear to be different if an importing Member establishes a safeguard in response to currently existing damage or damage that will most likely occur in the near future.[54] In addition, as the United States discussed, past panels interpreting Article 6 have not provided clear guidance.[55]

66. Nevertheless, Article 6 does provide some "parameters" with respect to an analysis of actual threat of serious damage. In particular, Article 6 requires a Member to base its assessment of actual threat of serious damage on (1) the eleven economic variables set out in Article 6.3 – recognizing that "none of which, either alone or combined with other factors, can necessarily give decisive guidance" – and (2) as set out in Article 6.7, specific and relevant factual information that is as up to date as possible. As reflected in the Market Statement and as

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short staple ring spindles) International Textile Manufacturers Federation, *International Textile Machinery Shipment Statistics*, Volume 20, 1997, Tables 1.3, 1.4, and 1.5. Furthermore, according to statistics published by the International Cotton Advisory Committee in 1998, Pakistan's production capacity of cotton yarn in 1997 was 1.5 million metric tons, more than three times Mexico's production capacity of cotton yarn, at 400 thousand metric tons. International Cotton Advisory Committee, *World Textile Demand*, 1998.

[53] First written submission of the United States, note 108.

[54] First written submission of the United States, at ¶¶ 110-112.

[55] First written submission of the United States, at ¶¶ 111-112. The Panel in *United States - Underwear* expressed that a finding of actual threat of serious damage requires a demonstration that, unless action is taken, damage will most likely occur in the near future. *United States - Underwear*, at ¶ 7.55. In contrast, the Panel *United States - Wool Shirts* declined to consider "whether serious damage or actual threat thereof is a single concept; whether serious damage is a short hand for the expression 'serious damage or actual threat thereof'; whether actual threat of serious damage is but a lower level of serious damage; whether the two expressions refer to different types of market situation in the importing market." *United States - Wool Shirts*, at ¶ 7.53

explained in the first written submission of the United States, the United States clearly fulfilled these requirements.[56]

67. Specifically, the United States conducted an analysis of actual threat of serious damage separate from its analysis of serious damage and focused on the impact that the surge in Category 301 imports would likely have in the immediate future. For this purpose, the United States examined objective and verifiable data for the factors contained in Article 6.3 – particularly data reflecting the most recent January-August 1998 period when the surge of Category 301 imports was at its height and most damaging. In other words, this analysis specifically focused on the negative trends in the months prior to the safeguard action[57] and reflected the latest available data, which for imports was current through October 1998, and for the other variables, was current through August 1998.[58] Based on this fact-based, up-to-date information, the magnitude of the most recent surge (total imports surged 91.3 percent and imports from Pakistan surged 283.2 percent), the low prices of imports compared to the average U.S. price, the likelihood that combed cotton yarn would continue to enter into the United States at such low prices, and the dire condition of the domestic industry, the United States concluded that the economic variables for the industry would continue to decline and accordingly that the industry faced an actual threat of serious damage and an exacerbation of the current serious damage from the increased imports of combed cotton yarn.[59]

68. In sum, in contrast to Pakistan's claim in its first written submission that the U.S. analysis of actual threat of serious damage amounted to a mere assertion,[60] the United States conducted its assessment of actual threat of serious damage based on a future-oriented analysis of the Article 6.3 factors which reflected the most up-to-date data available. Accordingly, the United States fulfilled the "parameters" required by Article 6 for such an analysis.

15. Please explain in further detail the position contained in paragraph 49 of the US First Submission. Please further explain your view that a Member is free to choose only one of the options listed in the paragraph.

69. The text of Article 6.2 of the ATC provides that "safeguard action may be taken under this Article when, on the basis of a determination by a Member, it is demonstrated that a particular product is being imported into its territory in such increased quantities as to cause serious damage or actual threat thereof to *the domestic industry producing like and/or directly*

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[56] *See* Market Statement, at ¶¶ 8.1-8.7 and first written submission of the United States, at ¶¶ 108-117.

[57] Market Statement, at ¶ 8.4 ("Every major benchmark of economic performance in 1998 is low and deteriorating. Profits, prices, shipments, market share, employment, capacity utilization and new orders are falling, while import penetration, inventories, and wages are rising."). *See also* Market Statement, at ¶ 8.5-8.7.

[58] First written submission of the United States, at ¶¶ 121-123.

[59] Market Statement, at ¶¶ 8.1-8.7.

[60] First written submission of Pakistan, at p. 40.

competitive products." As noted in paragraph 49 of the first written submission of the United States, this ATC language, if read alone, "would allow a Member to identify an industry producing a product that is: 1) like and directly competitive; 2) like but not directly competitive; or 3) unlike but directly competitive."

70. Generally accepted principles of treaty interpretation, reflected in Article 31 of the *Vienna Convention*, uphold this approach.[61] As explained *supra* in the answer to Question 2, the *New Shorter Oxford English Dictionary defines* "and/or" as "either together or as an alternative." Therefore, the ordinary meaning of the phrase "like and/or directly competitive" permits a Member, in analyzing a domestic industry, to choose from three potential definitions of domestic industry. First, the industry producing *like* products. Second, the industry producing *like and directly competitive* products." Third, the industry producing *directly competitive* products that are not *like*.

71. Nothing about the context or the object and purpose of the ATC suggests that the ordinary meaning of the phrase "like and/or directly competitive" would disallow one or the other of these three possibilities. The ATC could have drawn from other agreements which had defined domestic industry in another manner. Yet the ATC draws directly from the MFA and incorporates its "and/or" phrase.[62] Given this apparently intentional selection of this phrase, it should not be interpreted in a manner that nullifies any part of the meaning of the phrase absent some compelling reason based on the purpose and intent of the ATC.

72. As discussed *supra* in the answer to Question 3, the object and intent of the ATC supports crediting the full meaning to the phrase "like and/or directly competitive" products. The ATC is a special ten-year transitional agreement designed to phase out the special regime that governed trade in the textile and apparel sector under the MFA and gradually integrate the textiles and clothing sector into the disciplines of the GATT. The ATC – and particularly the Article 6 transitional safeguard mechanism – set forth a careful balancing of interests between exporting and importing Members.[63] On the one hand, exporting Members have security that, at the end of the ten years, all textile products will be subject to normal GATT rules. On the other hand, importing Members have protection against damaging surges in imports during the transition period from products which have not yet been integrated into GATT disciplines.

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[61] Article 31of the *Vienna Convention on the Law of Treaties* calls for the interpretation of a treaty "...in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in the light of its object and purpose."

[62] In fact, as discussed *supra* in the answer to Question 4, the fact that the ATC carried over the phrase "like and/or directly competitive" is very significant, particularly given the importance of the term "directly competitive" to paragraph 24 of the 1986 Protocol of Extension of the MFA.

[63] Report of the Appellate Body, *United States - Wool Shirts*, at p. 19, quoting *United States - Underwear*, at p. 15.

73. The ATC's purpose as a transitional agreement is not impaired by crediting the full meaning to the phrase "like and/or directly competitive." Indeed, giving the phrase the full range of its ordinary meaning is consistent with the transitional nature of the ATC and the assurance that a safeguard mechanism would be available during the transitional period. To discredit the ordinary meaning of that phrase would, in the view of the United States, amount to rewriting the carefully negotiated bargain struck in the ATC.

74. In sum, the plain language of the ATC permits a Member to identify an industry that is producing a like and directly competitive product, a like product, or a directly competitive product. This interpretation does not enable a Member to pick and chose which domestic industry it wants to consider in any manner that is not contemplated by the Agreement itself. Nor does is create an open-ended approach to the identification of the domestic industry. The ATC has set the scope of what can be considered the domestic industry as being the domestic industry producing like and/or directly competitive products. The U.S. approach in this case merely accords with that scope by focusing on the domestic industry producing the directly competitive product, i.e., the combed cotton yarn for sale industry. The United States took this approach because it reflected the realities of this particular market and because the United States would otherwise have been unable to consider all the factors set forth in Article 6.3.

Question 16: *Please discuss in detail the issue of "damage" to the subject domestic industry in the following situations:*

(a) A US manufacturer of combed cotton yarn for sale has been acquired by a "verticially integrated" firm and continues to produce the same product but only for the internal use of the integrated firm. The acquired manufacturer has maintained the same number of facilities.

(b) A vertically integrated firm is selling more combed cotton yarn in the market than de minimis, for example, 20%. It maintains the same level of production, but has recently switched a significant amount of its production to its own internal use.

(c) If a vertically integrated firm is now selling more than de minimis into the merchant market, how is that producer counted, i.e., wholly or partially within the subject "domestic industry"? If partially counted, how would this be done (with respect to relevant economic variables, e.g. productivity, utilization of capacity, inventories, wages, employment, profit and investment?

75. The United States notes as an initial matter that the U.S. transitional safeguard action on imports of combed cotton yarn products in Category 301 from Pakistan was based on the facts, circumstances and analysis set forth in the Market Statement. As presented in the Market Statement, the United States verified that there is minimal overlap, or interchange, between the domestic industry producing combed cotton yarn for sale and the vertically integrated producers

of fabric, apparel, or home furnishings, which manufacture combed cotton yarn for their own consumption in the production of these other end products. Therefore, the situations described in scenarios (a) and (b) did not exist during the period of investigation as a matter of fact. The United States offers the following responses to these scenarios in an effort to assist the Panel's thinking, but must emphasize that the responses are necessarily speculative.

76. A damage/threat analysis under the ATC starts with Article 6.2 when "it is demonstrated that a particular product is being imported into [a Member's] territory in such increased quantities as to cause serious damage, or actual threat thereof, to the domestic industry producing like and/or directly competitive products." Then, as Article 6.3 requires, in making a determination of serious damage, or actual threat thereof, a Member must "examine the effect of those imports on the state of the particular industry, as reflected in changes in such relevant economic variables as output, productivity, utilization of capacity, inventories, market share, exports, wages, employment, domestic prices, profits and investment; none of which, either alone or combined with other factors, can necessarily give decisive guidance."

77. The damage analysis that would occur in situations such as scenario (a) and (b) would not occur in a vacuum. Absent from the description of scenario (a) are facts regarding total imports which must, according to Article 6.2, be considered. In the particular case of the transitional safeguard action on combed cotton yarn in Category 301 from Pakistan, the United States registered an overall increase in Category 301 imports from all sources in excess of 90 percent during the latter part of the period of investigation. Furthermore, Article 6.3 clearly provides that no one industry-related variable, either alone or in combination with another factor, can necessarily give decisive guidance. Thus, the decline in production and changes in derivative statistics that would result if a "yarn for sale" firm were acquired by a vertically integrated fabric producer would not necessarily, on their own, result in a finding of serious damage/actual threat thereof. There may be many reasons for the situations described in scenarios (a) and (b) to occur, one of which might be that the sales yarn facility could no longer sustain viable production in the face of surges in low-cost imports. There may be other reasons why a vertically integrated mill might acquire a sales yarn facility, completely independently of the reasons for a damage/threat analysis, such as the opportunity to enter new markets. Accordingly, the broader context of the changes in the industry that could lead to scenarios (a) and (b) would also be considered.

78. In an economically sterile, laboratory-type environment, if the situation described in scenario (a) were to occur, then the official production statistics of the U.S. Census Bureau would reflect on the one hand a decline in production of combed cotton yarn for sale and on the other hand an increase in the production of combed cotton yarn for own use, in quantities which reflect the output of the firm that has changed ownership. Focusing on the statistics reflecting the for sale yarn industry, the statistics that are derived from the production statistics (for example, shipment statistics, the apparent domestic market, domestic market share, and the import-to-production ratio) would also reflect this change. The apparent domestic market would decline; the domestic market share would decline and the ratio of imports-to-production would increase, all other things being equal. The employment data would also show a decline. An industry

survey of some of the other Article 6.3 variables may also reflect that one firm exited the sales yarn industry (for example, the figures on inventories). The exiting of one firm from the sales yarn industry, however, may not be reflected in statistics on profits, productivity, unfilled orders or capacity utilization.

79. The situation described in scenario (b) is similar. If a vertically integrated fabric mill were selling more than *de minimis* quantities of yarn in the market and then switched to consume that yarn internally rather than to sell it on the market (which again, was not a situation that was present in the facts and analysis contained in the Market Statement), then the official production data would show a decline corresponding to the quantity of yarn no longer produced "for sale;" and the derivative statistics would also reflect the change. Again, all other things being equal, shipments would be lower, the apparent domestic market would decline; the domestic market share would decline and the ratio of imports-to-production would increase. The employment data would probably also show a decline, although this change can be assumed to be marginal given the facts outlined in scenario (b). An industry survey of some of the other Article 6.3 variables may also reflect that one firm exited the sales yarn industry (for example, the figures on inventories). The transferring of quantities of yarn from "for sale" to internal consumption may not be reflected in statistics on profits, productivity, unfilled orders or capacity utilization.

80. Again, an analysis of the existence or threat of serious damage in situation such as that described in scenario (b) would not occur in isolation. Even assuming that a 90-plus percent increase in overall imports was present in scenario (b), the decline in production and changes in derivative statistics that would result if a vertically integrated firm shifted yarn previously offered for sale on the market to internal consumption would not necessarily, on their own, result in a finding of serious damage/actual threat thereof. However, again as noted, the particular situation described in scenario (b) did not exist at the time of the U.S. investigation and was therefore not a part of the pattern of facts and circumstances, and the United States would reiterate that its verification of the overlap between the sales yarn industry and the fabric/home furnishings industry producing yarn for internal consumption did not reveal that vertical fabric, apparel, and home furnishings producers sold the equivalent of 20 percent of their production in the market.

81. The United States conducted a representative survey of vertically integrated fabric, apparel, and home furnishings producers and found that they sell only a *de minimis* amount (roughly one percent) of the combed cotton yarn they manufacture on the open market. In theory, if there were such a producer as described in (c), that producer's shipments to the for sale market would be reflected as such in the official U.S. Bureau of Census production statistics. If the producer were a true vertically integrated facility, then the AYSA survey of variables that are not reported to the Census Bureau – such as productivity, utilization of capacity, inventories, profit and investment – might not reflect the extent of the vertically integrated facility's new venture into the sales market.

82. However, it should be noted that the verification of the AYSA data against the official Census data undertaken by the U.S. ensured that the data presented in the Market Statement was

complete, accurate and reliable. For example, if one were to compare production data for 1996 and 1997, which was available in both the AYSA survey and the Census data, one would find that the AYSA production data was actually slightly higher than the Census Data, but the difference was *two-tenths of one percent* in each year,[64] and the level of decline was the same for both sets of data. The U.S. is confident, therefore, that the situation described in scenario (c) did not exist at the time the Market Statement was prepared, and that the data represented, uniformly, a picture of the combed cotton sales yarn industry.

Question 17: *Please explain the basis for the adoption by the US authority of the "best information available" standard. What is the exact definition of this term used by the United States in the context of the ATC? In this connection, please explain whether and how exporting Members are given the opportunity to present their views and supporting evidence in the US investigation procedures.*

83. The United States did not intend to imply in its first written submission that the "best information available" was a standard required by the ATC. Rather, in the absence of any specific requirement for the collection of data set out in the ATC, the United States was making the factual statement that it relied on the best and most reliable information available to it in the preparation of the Market Statement. In addition, the United States did not intend to imply that its data collection ended with whatever statistics were available. Rather, as discussed in the first written submission, the United States verified all data it received from the private sector to the extent possible to ensure its accuracy and consistency with official statistics.

84. The ATC sets forth no requirement for the collection and analysis of data and affords the importing Member discretion in establishing its methodology, including relying on data furnished by the private sector.[65] Article 6.7 of ATC only requires that the Member accompany its request for consultations with specific, relevant, and current factual information related, as closely as possible, to identifiable segments of production and to the 12-month reference period. As discussed in its first written submission, the United States fully complied with these requirements.[66] U.S. data was as up-to-date as possible – reflecting data for 1996, 1997, and the first eight months of 1998 and including the most current import data through October 1998. The data enabled the United States to evaluate the level of imports and the effect of the increase

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[64] This difference could be explained by the methodology and frequency with which AYSA collects production data. AYSA collects for sale yarn production data from its members on a monthly basis, and this data is collected in pounds. AYSA converts the pounds data into kilograms using a conversion factor of 2.2 pounds per kilogram. This results in a slightly larger number than if one were to apply the official U.S. conversion factor of 2.2046 pounds per kilogram.

[65] *See United States - Wool Shirts*, at ¶ 6.4 ("...we reiterate that we do not interpret the ATC so as to impose on WTO Members any method of collecting data but that it is up to each concerned Member to collect the relevant data from relevant sources, *possibly including the private sector*." (emphasis supplied)).

[66] First written submission of the United States, at ¶¶ 144-147.

in imports of combed cotton yarn on the defined domestic industry, as reflected in such economic variables as output, productivity, capacity utilization, inventories, market share, exports, wages, employment, domestic prices, profits and investment.

85. The ATC – unlike the Safeguards Agreement and other non-transitional WTO agreements – does not establish specific requirements for a public notice and comment period during the pendency of the investigation.[67] Article 6.7 of the ATC only requires that the "Member proposing to take safeguard action...[to] seek consultations with the Member or Members which would be affected by such action" and to accompany that request for consultations with specific and relevant factual information as up-to-date as possible. The United States fulfilled this requirement when it requested consultations with Pakistan regarding Category 301 imports of combed cotton yarn from Pakistan and accompanied this request with the Market Statement, which contained specific, relevant, and current information with respect to the economic variables contained in Article 6.3 and the factors relating to attribution set forth in Article 6.4. Although not required by the ATC, the United States also provided public notice and solicited public comments on its request for consultations with Pakistan regarding Category 301 imports of combed cotton yarn.[68]

86. The ATC does not require a consideration of the views of exporting Members beyond what is set out in Article 6. The United States believes that it would be inappropriate for the Panel to impute requirements from non-transitional WTO agreements – such as specific notice and comment procedures – into the text of the ATC. As the United States discussed in its first written submission, the ATC and non-transitional WTO agreements were drafted in different ways and use different language, and the ATC has a fundamentally different purpose from other non-transitional WTO agreements.[69] In addition, neither the text of nor the practice under the MFA – which informs the context for interpreting Article 6 of the ATC – included such a requirement. The absence in Article 6 of the ATC of the public notice and comment procedures found in other agreements strongly suggests that such requirements did not constitute a part of the ATC's carefully negotiated balance of rights and obligations between exporting and importing Members.

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[67] *Compare* ATC, Art. 6 (which includes no notice and comment requirements for purposes of the transitional safeguard mechanism) *to* Safeguards Agreement, Art. 3 (which requires "reasonable public notice to all interested parties and public hearings or other appropriate means in which imports, exporters and other interested parties could present evidence and their views...") *See also* Antidumping Agreement," Art. 6 and *Agreement on Subsidies and Countervailing Measures* (the "SCM Agreement), Art. 12.

[68] 63 *Federal Register* 72288 (31 December 1998), which was attached to the first written submission of the United States as U.S. Exhibit 2 ("U.S.-2"). The United States publishes all federal rules, proposed rules, public notices, and request of public comments in the *Federal Register*.

[69] First written submission of the United States, at ¶¶ 57-62, 93, 99.

Question 18: *Have US manufacturers made direct investment in combed cotton yarn producers in Mexico? Please describe and quantify.*

87. To our knowledge, U.S. manufacturers did not make direct investments in combed cotton yarn production in Mexico during the period of investigation.[70]

Question 19: *Did the United States determine whether there was a long-term price differential between imports from Pakistan and from other sources (including specifically Mexico)? If so, what was the answer? If not, why not? If not, how was the comparative analysis done to determine that serious damage from imports was properly attributable?*

88. Article 6 does not require a Member to conduct an analysis of long-term price differentials between other sources. Rather, Article 6.4 of the ATC requires that a Member examine "import and domestic prices at a comparable stage of commercial transaction" as part of its determination of attribution. In addition, Article 6.7 requires information with respect to the factors in Article 6.4 be "as up to date as possible" and related, as closely as possible, to identifiable segments of production and to the 12-month reference period set out in Article 6.8. Given the requirements of Articles 6.4, 6.7, and 6.8, the United States did not make a determination as to whether there was a long term price differential between imports from Pakistan and from other sources, including Mexico.

89. In complying with the requirements of Articles 6.4, 6.7 and 6.8, the United States looked at the average landed duty-paid value of imports of Category 301 from all sources, including Mexico and other FTA partners, during the period January-August 1998. The United States determined that Pakistan was the lowest-priced of the leading, uncontrolled suppliers of Category 301 imports. The Market Statement reflects that Pakistan is a low-cost supplier of Category 301 products to the United States, with an average landed duty-paid value of $3.63 per kilogram – 26.2 percent below the average U.S. producers' price ($4.92 per kilogram) and 20 percent below average world prices ($4.54 per kilogram).

90. In response to a question that was presented during the TMB review, the United States provided detailed information on the price of Category 301 imports from Mexico.[71] This information revealed that Category 301 imports from Mexico entered the United States at an average landed duty-paid value of $3.96 per kilogram during the first eight months of 1998, 19.5 percent below the average U.S. producers' price and 9.1 percent above Pakistan's price to the

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[70] During the course of the TMB review of the U.S. transitional safeguard measure on Category 301 imports from Pakistan, Pakistan alleged that a U.S. producer of combed cotton yarn had set up a production facility in Mexico. However, the United States informed the TMB that this production facility would produce *carded cotton yarn*, not combed cotton yarn, and that this yarn was not imported into the United States. As the United States has discussed, carded cotton yarn is a separate product and is classified by United States as Category 300.

[71] *See* Written Answers to Questions from Pakistan, at ¶ 19.

U.S. market. Furthermore, Category 301 imports from Mexico were 12.8 percent below the average landed duty-paid value of Category 301 imports from all sources.

Question 20: *What are the similarities or differences in the quality/technical specifications of the domestically produced combed cotton yarn for sale and for internal use, the imports from Pakistan and the imports from Mexico?*

91. Some variations in quality are characteristic of goods on the marketplace, whether domestically-produced or imported, although quality is somewhat subjective. Generally, however, combed cotton yarn on the marketplace, whether domestically produced or imported (from any source) is of similar and comparable quality. To the best of our knowledge, there are no material differences in the technical specifications of the yarn produced domestically for sale, for internal use and the yarn imported from Pakistan or Mexico.

United States - Transitional Safeguard Action on Combed Cotton Yarn from Pakistan

Answers to Written Questions from Pakistan

1. The United States provides below answers to the nine written questions posed by Pakistan. The United States notes that many of these questions use terminology and concepts that do not appear in the Market Statement or in the parties' first written submissions. In addition, the questions appear to be based on a misreading of claims made by the United States in its first written submission and a misunderstanding of the conditions that actually exist in the relevant industries. At a minimum, use of these new terms and concepts invites confusion on behalf of the United States and the Panel. The United States has made its best effort to understand the basis for Pakistan's questions and to answer those questions accordingly.

2. The United States would also note that most of the written questions from Pakistan concern the production data collected by the United States during its investigation. As the United States explained in the Market Statement and its first written submission, the United States relied on production data supplied by the American Yarn Spinners Association ("AYSA"), and verified these statistics based on official U.S. Bureau of Census data.[1] U.S. Census data for yarn is reported in two categories: yarn "for sale" and yarn "for own use." The AYSA statistics and the U.S. Census data provided remarkably similar results for "for sale" yarn, and both demonstrated that production of Category 301 "for sale" yarn was declining – a fact Pakistan does not dispute.

Question 1

The USG has excluded three types of yarns from the definition of "for sale yarn", i.e.

1. *For own use yarn,*
2. *Yarn manufactured "on commission",*
3. *Yarn shipped to "affiliated companies".*

These three types of yarn are excluded from the USG analysis of the industry as USG has defined it. We have following question in this regard:

> *Why should "on commission yarn" and "yarn supplied to affiliated companies", whatever the quantities, not be counted with "for sale yarn"?*

3. The United States based its identification of the domestic industry as the "combed cotton yarn for sale" industry on the approach that has been taken by the U.S. Census Bureau since 1959. The U.S. Census Bureau's Current Industrial Report (CIR) series on Yarn Production

[1] Market Statement, at ¶ 1.4; first written submission of the United States, at ¶ 150.

(MA313F) covers the production of spun yarns.[2] Currently, this report divides yarn data into two categories: "for sale" and "for own use or on commission." These two categories distinguish between (1) yarn that participates directly in the marketplace and is subject to all the influences of the market and (2) yarn that does not enter the marketplace and thus is insulated from the direct effects of market forces. In the CIR series, "for own use" includes yarn consumed at the same plant where the yarn is produced, and yarn consumed by affiliated plants (e.g., those whose parent owns a majority interest in the spinning plant). In its Article 6 analysis, the United States made the same distinction used by the U.S. Census Bureau when it identified the "domestic industry" as the "combed cotton yarn for sale" industry and excluded yarn that would be reported to the Census Bureau as "for own use "and consumed internally by the fabric industry.

4. Pakistan has asked why yarn consumed at "affiliated companies" and yarn "on commission" is not included in "for sale" yarn. The short answer, which is further explained below, is that such yarn does not enter the market and does not directly compete with other yarn – whether imported or domestic.

5. As discussed above, the U.S. Census Bureau category "for own use" includes yarn consumed at the same plant where spinning occurs. It also includes yarn consumed by an affiliated company. The U.S. Census Bureau defines "affiliated company" based on ownership or control of the majority of the voting stock of a company, or based on a common parent owning or controlling the majority of the voting stock of both companies. Where a spinning plant supplies yarn to a company under the same ownership or under the ownership of a company holding a majority interest in the spinning plant, any transaction that takes place (if one takes place at all) occurs outside the market forces associated with the "for sale" market. While the corporate structure may be more complex where the yarn is consumed at an affiliated company, the consumed yarn bears the same relationship to the "for sale" market as is the case when yarn is consumed at the plant where the yarn is spun. The consumed yarn does not enter the "for sale" yarn market. For this reason, yarn consumed at an "affiliated company" is properly excluded from "for sale" yarn.

6. With respect to combed cotton yarn, yarn "on commission" is an obsolete term. From 1959 (the first year the CIR on yarn production was published) through 1985, the report included a separate data column for yarns spun "on commission." With respect to combed cotton yarn, the last year any commission shipments were reported was 1979; in that year, only 500,000 pounds of spun machine knitting yarn were reported, which is just three tenths of one percent of all combed cotton spun machine knitting yarn, and is an even smaller percentage of total combed cotton yarn spun.

7. From 1980 through 1985, the CIR reported that no combed cotton yarn was manufactured

[2] The United States provided an excerpt of the 1997 *Current Industrial Report* for Yarn Production as U.S. Exhibit 9 (U.S.-9).

on commission. Since no data were reported for these years, Census collapsed the data columns "on commission" and "for own use" into a single column.

Question 2

a) What is the definition of an affiliated company?

8. As discussed in Question 1, the U.S. Bureau of the Census defines "affiliated company" based on ownership or control of the majority of the voting stock of a company, or based on a common parent owning or controlling the majority of the voting stock of both companies.

b) Is it a separate corporate entity?

9. An affiliated company can be a company that owns another company or controls the majority of the voting stock of another company. Or, an affiliated company could be one that shares a common parent which either owns both companies or owns or controls the majority of the voting stock of both companies.

c) Does an affiliated company purchase yarn from the "for sale yarn" market also?

10. An "affiliated company" could be a fabric company that gets all its yarn from its affiliated yarn spinning company, or it could be one that purchases all its yarn from the "for sale" market, or it could be a company that does not produce a product that uses yarn at all.

d) Is the shipment of yarn made to an affiliated company considered a "sale transaction", with accompanied "sales invoice" with a "sale price"?

11. Transfers between affiliates would be noted in some form for accounting purposes. Often transfers are noted as "inter-plant transfers." However, given the various relationships that are covered by "affiliated company," this question cannot be answered more specifically.

e) Are state and federal taxes, including income tax, leviable on sales to affiliated company?

12. Again, given the various relationships that are covered by "affiliated company" and the complex and different tax structures of the federal government and the fifty state governments, this question cannot be answered in the abstract.

f) Do prudent management policies and state/federal fiscal agencies require that the purchase of yarn by affiliated companies be at competitive prices available in the market?

13. We are aware of no state or federal agency whose statutory mandate gives it the authority to establish the price for yarn purchases between affiliated or non-affiliated companies at the price available in the market.

Question 3: *Are "heather yarn" and "dyed cotton yarn", combed, chiefly cotton covered under category 301 and subject to the restraint?*

14. To the extent that heather yarn and dyed cotton yarns are of chief weight cotton combed yarns, they would be included in the U.S. Harmonized Tariff Schedule (HTS) headings that comprise Category 301 and would be subject to the transitional restraint on imports of Category 301 products from Pakistan. Footnote 1 to the Market Statement identifies the 38 headings of the HTS of the United States that comprise Category 301.[3] Of course, as was discussed extensively before the Textiles Monitoring Body, "heather yarn" of carded cotton fiber would not be included in Category 301, nor would "dyed cotton yarn"of carded cotton fiber.

Question 4: *USG has stated that integrated units with a "separate sales division" are members of AYSA.*

a) Do companies with several yarn producing establishments assign some of the establishment to the "separate sales division" and remaining to "integrated division". Or is "separate sales division" really a term describing "yarn sales department" which can sell yarn produced by any of the company's establishments?

b) Can the "integrated division" procure yarn from the so-called "separate sales division" and, if so, would you count this quantity in your "de minimis" procurement from the "for sale" market or an "own use" procurement?

c) Can an integrated company with only one yarn spinning establishment have a "separate sales" division?

15. The United States does not use the term "integrated units" or "integrated divisions" and does not know what Pakistan intends these terms to cover. The United States assumes that Pakistan means to refer to "vertically integrated fabric producers." If so, it has misread the United States' first submission and has based its question on that misreading. The United States did not state, as Pakistan's question implies, that vertically integrated fabric producers with a

[3] The United States supplied a correlation of Category 301 with relevant HTS numbers at U.S. Exhibit 1 ("U.S.-1").

separate sales division are members of AYSA. To be a member of AYSA, an establishment must be dedicated to yarn spinning for sale. Vertically integrated *fabric producers* are not establishments dedicated to producing yarn for sale and are not members of AYSA. Many of AYSA members are stand alone yarn spinning establishments. Other members of AYSA are separate divisions of larger companies. Separate divisions of larger companies can be members of AYSA if the divisions are dedicated to yarn spinning for sale. What the United States stated in its First Submission in this regard, which appears to have been misread by Pakistan, is the following:

> AYSA is the national trade association for the sales yarn industry and does not represent the interests of vertically integrated fabric producers manufacturing combed cotton yarn for their own consumption. AYSA membership includes five firms that produce fabric and yarn for sale *in separate divisions*. Each separate division represents a distinct profit center within the corporation. Each division would also report its production data separately. Therefore, the inclusion of these five firms in the AYSA survey was appropriate because, although these sales yarn establishments share a corporate parent with fabric establishments, their production of sales yarn is *separate* from and not for the exclusive use of their sister vertically integrated fabric establishments. Thus, the separate yarn for sale divisions of the five producers included in AYSA's membership are legitimately part of the defined yarn for sale industry.[4]

16. Additionally, it may be helpful to note that when the United States refers to yarn sales divisions and fabric divisions, it is using the term "division" as it is typically used to refer to business units within companies. For example, the term "division" has been explained as follows:

> A business unit is an organizational entity that operates in a distinct business area. Typically, it is self-contained and has its own functional departments (for example, its own finance, purchasing, production, and marketing departments). Within most companies, business units are referred to as **divisions.**[5]

17. Because Questions 4a-4c are based on this misreading of the U.S. position and a misunderstanding of the relationships that actually exist in the industry, the United States is unable to respond with any more specificity to these questions. Our hope is that a better understanding of the U.S. statement set out above will resolve these questions in their entirety.

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[4] First written submission of the United States, at ¶ 73. (footnote omitted)

[5] Charles W.L. Hill and Gareth R. Jones, *Strategic Management: An Integrated Approach* (New York, 1998)(bold in the original).

Question 5: *In answer to a TMB member, USG circulated a price comparison report, "Average Landed Duty Paid Value of Imports, Yarns for Sale, Chief Weight Combed Cotton Spun, Category 301" for January-August 1998, Pakistan yarn at $3.63/kg and Mexico yarn at $3.96/kg. When the TMB member enquired about the reason why Mexico yarn sales are growing at a faster rate than Pakistan yarn sales, USG replied that it was because of preferential tariff/quota treatment given to textile goods made out of Mexican yarn. Is this information correct?*

18. The United States has been unable to confirm Pakistan's claim regarding U.S. statements to the TMB. Nevertheless, there could be a variety of reasons for growth in Mexican yarn sales, and any attempt to isolate a particular reason would be speculative.

19. As to the price comparison table, at the TMB review of the U.S. transitional safeguard measure on Category 301 imports from Pakistan, the United States was asked by TMB members to provide information on the average landed duty-paid value of imports of Category 301 with respect to certain Members. The United States complied with this request, and provided the following table:

Average Landed Duty-Paid Value of Imports
Yarn for Sale, Chief Weight Combed Cotton Spun
Category 301

Supplier	January-August 1998 Unit Value ($ per Kilogram)
World	$4.54
Mexico	$3.96
Pakistan	$3.63
Egypt	$5.92
Thailand	$3.76
Indonesia	$4.07
Malaysia	$4.22
Italy	$7.69
Peru	$8.07
Korea	$3.50

China, Taiwan	$3.43
Turkey	$4.43
Canada	$4.78
El Salvador	$4.26
Philippines	$3.17
Japan	$7.14
Switzerland	$11.32

Source: U.S. Census Bureau.

20. This information was consistent with the U.S. determination to attribute serious damage, or actual threat thereof, to Pakistan, as imports from Pakistan were the lowest-priced of any leading unrestrained supplier of Category 301, with an average landed duty-paid value of $3.63 per kilogram during the first eight months of 1998 – 26.2 percent below the average U.S. producers' price. As this table demonstrated, at the time of the transitional safeguard action, imports of Category 301 from Mexico were significantly higher priced than imports from Pakistan.

Question 6: *Is it possible to determine from US Bureau of Census data, which gives yarn "for sale" and "for own use & commission", how much of the quantity listed under "for sale" was sold by integrated units?*

21. Again, we are unclear what Pakistan means by "integrated units" but will assume that this term means "vertically integrated fabric producers." No, it is not possible, using Census data alone, to determine how much of the quantity listed under "for sale" was sold by vertically integrated fabric producers. The U.S. Census Bureau does not break out the amount of combed cotton yarn that is produced by individual establishments, nor does it divide establishments based on whether they are vertically integrated fabric producers or producers of combed cotton yarn for sale. Under U.S. law, the U.S. Census Bureau is obligated to protect confidential business information from disclosure, even to other U.S. Government agencies, and thus reports its data in a format that protects such information from disclosure.

Question 7: *Para 69 on page 24 of the US first submission states that the USG "conducted a representative survey of eight large integrated mills". How many of these eight mills have a "separate sales division"? How many of these eight mills were member of AYSA?*

22. The United States conducted telephone interviews with eight vertically integrated producers of fabric, apparel, or home furnishings to determine the extent to which these establishments purchase or sell combed cotton yarn on the open market. Based on these discussions, the United States determined that vertically integrated fabric producers purchase roughly two percent of their yarn requirements on the market and sell roughly no more than one percent of the combed cotton yarn they spin on the market.[6]

23. The United States did not inquire if the eight mills have "separate sales divisions" or if they are members of AYSA. The United States has since determined that two of the companies it surveyed regarding vertically integrated fabric, apparel and home furnishing production also maintain a separate division dedicated to the production of combed cotton yarn for sale. The latter divisions dedicated to the production of combed cotton yarn for sale are both members of AYSA.

Question 8: *Footnote 66, on page 26 of the US first submission states that " . . . . . the hypothetical division that produces yarn for sale would report its yarn as yarn for sale". Is all the yarn produced by this hypothetical division reported as "yarn for sale" or the part that is shipped to a sister fabric company reported as "for own use"? What percentage of yarn requirement of integrated units is obtained from their own "separate sales division"?*

24. The hypothetical division discussed in footnote 66 is described simply as a division that produces combed cotton yarn for sale. This hypothetical division is intended to represent the norm. Applying that hypothetical norm to the questions posed, the answers are the following. All yarn produced by this facility is reported as "yarn for sale" and none is shipped to a sister vertically integrated fabric producer and reported as "for own use." This hypothetical company's sister vertically integrated fabric producer produces yarn sufficient for its own needs and does not rely on its sister yarn spinner division for its yarn needs.

Question 9: *What percentage of yarn requirement of integrated units is obtained from their own "separate sales division"? What is the source of this information and if it is the result of a survey, when was this survey undertaken and how many companies were surveyed?*

25. Again, the United States assumes that Pakistan means "vertically integrated fabric producers" when it refers to "integrated units." The United States also assumes that Pakistan is asking what percentage of yarn vertically integrated fabric producers consume is obtained from affiliated yarn spinning companies. The United States is not aware of how much yarn vertically integrated fabric producers obtain from affiliated companies dedicated to yarn spinning for sale. However, as noted above and in the Market Statement, vertically integrated fabric producers seek

[6] *See* first written submission of the United States, at ¶ 69.

to balance the manufacture of yarn and fabric and rarely go outside the vertically integrated structure to source yarn from either the market or affiliated companies.

U.S. EXHIBIT 10

Exhibit U.S. - 10

Paragraph 24 of the 1986 Protocol Extending the MFA

24. (i) The Committee acknowledged the concern of some importing countries regarding substantially increased imports of textiles made of vegetable fibres, blends of vegetable fibres with fibres specified in Article 12, and blends containing silk, which are directly competitive with textiles made of fibres specified in Article 12. Accordingly, the Committee agreed that the provisions of Articles 3 and 4 may be invoked with respect to directly competitive imports of such textiles, in which any or all of those fibres in combination represent either the chief value of the fibres or 50 per cent or more by weight of the products, which cause market disruption or a real risk thereof, bearing in mind also the provisions of Article 8, paragraph 3 of the Arrangement.

(ii) In examining the case for market disruption, the Textiles Surveillance Body is instructed to pay particular attention to the evidence demonstrating that these products are directly competitive with products of cotton, wool and man-made fibres manufactured in the importing country concerned.

(iii) It is understood that restraints will not be applied to historically traded textiles which were internationally traded in commercially significant quantities prior to 1982, such as bags, sacks, carpetbacking, cordage, luggage, mats, mattings and carpets typically made from fibres such as jute, coir, sisal, abaca, maguey and henequen.